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MERCANTILE STORES COMPANY, INC.

ANNUAL REPORT

JANUARY 31ST, 1937

MRS
CORP. FILE

15 Exchange Place,
Jersey City, New Jersey,
April 15, 1937.

To the Stockholders of

Mercantile Stores Company, Inc.:

Consolidated Balance Sheet as of January 31, 1937 and Consolidated Profit and Loss and Surplus Accounts for the year ended January 31, 1937 of your Company and its subsidiaries are submitted herewith.

The net profit for the year after providing for Federal income taxes amounted to $803,990.07 which is equivalent to $5.07 per share on the 149,125 shares of common stock outstanding in the hands of the public. The amount of $5.07 is after providing $47,796.00 for preferred stock dividends at $7.00 per share. For the preceding year, the net profit amounted to $120,486.04 which, after providing for preferred dividends, amounted to $.50 per share on the 144,125 shares outstanding at that time.

A dividend of $3.00 per share, aggregating $447,375.00 was paid on the common stock in January 1937 in Ten Year Five Per Cent (5%) Debentures of the Company dated January 20, 1937. The Company offered to pay to any stockholder for his Debentures, upon his written request, the principal amount of any such Debentures without interest on or before March 1, 1937. Pursuant to such offer, the Company purchased $143,751.00 principal amount of these Debentures.

The recent Ohio Valley flood caused a total suspension of business in three of our stores for a short period during January and February, 1937. Three other stores were temporarily affected. Use and occupancy insurance covered the stores against the loss of gross profit incurred while their business was affected by the floods. An agreement has been reached with the insurance company with respect to such losses, under which the stores will receive a total of $155,223.22, of which $104,334.00 is applicable to January 1937, and the balance of $50,889.22 is applicable to the year ending January 31, 1938. Of the amount applicable to January 1937, $74,334.00 has been included in the income of the year ended January 31, 1937 and $30,000.00 has been reserved to cover the approximate increase in the cost of similar insurance during the next three years.

Customers' receivables increased materially during the year, particularly installment accounts. Provision for losses has been made in accordance with the actual bad debt experience of the stores during the past five years.

For several years the management has maintained a conservative policy on inventory. Advancing prices and poor deliveries coupled with expanding retail sales have made it necessary for us to increase our inventory.

The Companies follow a policy of taking gross profit on installment sales into income at the time of sale but for Federal income tax purposes they report such gross profit as collected. In preceding years the provision for Federal income taxes has been recorded on the books in amounts equal to the tax reflected on the tax returns filed for the respective years. Owing to the substantial increase in installment sales and the consequent increase in the amount of gross profit deferred for income tax purposes, the Companies have provided a reserve for the amount of tax to be reported in the tax return of the current year, and have also created a reserve in the amount of $163,000.00 which, based upon present tax rates, is adequate to cover the estimated normal Federal income tax which may be payable in future years on all profits taken up in books but not yet reported in Federal income tax returns. This reserve of $163,000.00 was created by a transfer of $130,938.80 from the reserve for contingencies and by a charge against earnings in the amount of $32,061.20, the latter amount representing the additional normal tax which would have been reported in the tax return for the current year if no profit were deferred in reporting the income to the Government.

No provision was made for Federal surtax on undistributed profits which may be payable in subsequent years on the gross profit deferred at January 31, 1937. Under the present tax law, the Companies may or may not be required to pay a surtax on such income depending among other things, upon the amount of dividends which are paid in such future years in relation to the profits of such years.

Sales for the past year amounted to $30,814,092.80, an increase of 8.65% over the preceding year.

Sales of the new year to date are substantially ahead of the year just closed. However, operating expenses have been rising rapidly for the past few months and as a consequence a larger portion of our increased gross has been absorbed in increased expenses. A further factor in this connection is that in several of our stores where we operate in leased buildings, the terms of the lease agreements provide for increased rentals as sales and/or profits are increased.

The management wishes to express its sincere appreciation for the loyalty and efficient co-operation of all employees.

By Order of the Board of Directors,

F. G. KINGSLEY
President

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AND SUBSIDIA

CONSOLIDATED BALANC

ASSETS

CURRENT ASSETS:		
Cash in banks and on hand		$ 987,495.78
Customers' accounts receivable—		
Regular retail terms	$2,639,005.77	
Installment terms	3,830,177.36	
	$6,469,183.13	
Less—Reserves for doubtful accounts	590,891.39	5,878,291.74
Due from suppliers, amounts recoverable from insurance company, etc.		270,376.31
Merchandise inventories, quantities and condition determined by the companies—valued on the basis of cost or market, whichever is lower, as determined by the retail inventory method—		
On hand	$4,063,063.03	
In transit	537,872.82	4,600,935.85
TOTAL CURRENT ASSETS		$11,737,099.68
OTHER ASSETS:		
United States Government securities deposited in escrow as guarantee of performance of a lease—at cost (market value, $106,844.00)	$ 103,968.74	
Miscellaneous securities, etc.	27,919.16	131,887.90
FIXED ASSETS:		
Land and buildings owned and under purchase contracts, buildings on leased ground, and leaseholds (of which, property of the net book value of $270,502.01 is pledged to secure performance of a lease)—at cost, less depreciation of $1,767,902.24	$4,783,834.54	
Store fixtures—at cost, less depreciation of $1,135,192.93	1,166,792.52	
Delivery equipment—at appraised values as determined by the management	22,885.61	
	$5,973,512.67	
Land and buildings not used in store operations—at cost, less depreciation of $29,688.49	224,637.34	6,198,150.01
UNEXPIRED INSURANCE PREMIUMS, SUPPLY INVENTORIES, PREPAID EXPENSES, ETC.		246,998.70
		$18,314,136.29

NOTES:

(1) Contingent liability on customers' notes discounted –

(2) Surplus of $489,643.30 is restricted by reason of pu

ES COMPANY, Inc.

Corporation)

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SHEET—JANUARY 31, 1937

LIABILITIES

CURRENT LIABILITIES:		
Notes payable to banks		$ 1,500,000.00
Accounts payable—		
For merchandise	$1,122,530.42	
For merchandise in transit	537,872.82	
For expenses and sundries	575,428.58	2,235,831.82
Accrued taxes (other than Federal income), salaries, rent and interest		422,929.31
Mortgage and other real estate obligations payable within one year		72,733.34
Preferred stock dividend payable February 15, 1937		11,949.00
Reserve for increase in cost of flood insurance (see report to stockholders)		30,000.00
Reserve for Federal income taxes		121,000.00
Reserve for redemption of trading stamps issued by subsidiary company		56,930.03
TOTAL CURRENT LIABILITIES		$ 4,451,373.50
MORTGAGE AND OTHER REAL ESTATE OBLIGATIONS—		
Maturing after one year		312,199.92
TEN YEAR FIVE PER CENT DEBENTURE BONDS—Due 1947	$ 447,375.00	
Less—In treasury (repurchased in accordance with offer made to stockholders—see report to stockholders)	931.00	446,444.00
RESERVE FOR NORMAL FEDERAL INCOME TAX which may be payable in future years on gross profit deferred for Federal income tax purposes (see report to stockholders)		163,000.00
CAPITAL STOCK AND SURPLUS:		
Capital stock—		
Preferred stock—7% cumulative, $100 par value—callable at $105—		
Authorized and issued, 10,410 shares	$1,041,000.00	
Less—In treasury, 3,582 shares	358,200.00	$ 682,800.00
Common stock—no par value (stated value, $36.66⅔ per share)—		
Authorized and issued, 158,238 shares	$5,802,060.00	
Less—In treasury, 9,113 shares	334,143.33	5,467,916.67
Surplus segregated by the Board of Directors as of February 1, 1935, per attached statement		6,408,893.09
Earned surplus since February 1, 1935, per attached statement		381,509.11
		12,941,118.87
		$18,314,136.29

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hase of treasury stock until such stock is sold or canceled.

MERCANTILE STORES COMPANY, INC.
AND SUBSIDIARY COMPANIES

CONSOLIDATED PROFIT AND LOSS AND SURPLUS ACCOUNTS
For the Year Ended January 31, 1937

CONSOLIDATED PROFIT AND LOSS ACCOUNT

Net sales (including sales of leased departments)		$30,814,092.80
Cost of goods sold, selling, operating and administrative expenses, exclusive of depreciation		29,802,957.09
		$ 1,011,135.71
Other income (Net)—Carrying charges on installment accounts, miscellaneous income, etc. (including $74,334.00 of amount recoverable from insurance company for loss of gross profit resulting from floods—see report to stockholders)		309,756.42
		$ 1,320,892.13
Deduct:		
Depreciation	$312,127.94	
Interest expense	52,531.14	364,659.08
Net profit before provision for Federal income taxes		$ 956,233.05
Provision for Federal income taxes (including $8,000.00 representing surtax on undistributed profits)		152,242.98
Net profit carried to earned surplus		$ 803,990.07

SURPLUS SEGREGATED BY THE BOARD OF DIRECTORS AS OF FEBRUARY 1, 1935

Balance, January 31, 1936	$ 6,517,226.42
Deduct—Excess of stated value of 5,000 shares of treasury common stock over the price at which they were sold to an officer ($15.00 per share) in accordance with an option agreement dated October 29, 1935 (such stock had been acquired in preceding years at an average cost of $20.95 per share)	108,333.33
Balance, January 31, 1937	$ 6,408,893.09

EARNED SURPLUS SINCE FEBRUARY 1, 1935

Balance, January 31, 1936		$ 72,690.04
Net profit for the year ended January 31, 1937		803,990.07
		$ 876,680.11
Deduct—Dividends declared:		
Preferred stock—$7.00 per share, paid or payable in cash	$ 47,796.00	
Common stock—$3.00 per share, paid in Ten Year Five Per Cent Debentures	447,375.00	495,171.00
Balance, January 31, 1937		$ 381,509.11

ARTHUR ANDERSEN & CO.

ACCOUNTANTS AND AUDITORS

67 WALL STREET
NEW YORK

TO THE BOARD OF DIRECTORS OF
MERCANTILE STORES COMPANY, INC.:

We have made an examination of the consolidated balance sheet of Mercantile Stores Company, Inc. (a Delaware corporation) and subsidiary companies as at January 31, 1937, and of the consolidated profit and loss and surplus accounts for the year ended that date. In connection therewith, we examined or tested accounting records and other supporting evidence of the company and certain of its more important subsidiaries, and obtained information and explanations from officers and employees of the companies; we also made a general review of the accounting methods and of the operating and income accounts for the year, but we did not make a detailed audit of the transactions. The total assets of the companies whose records we examined represented 78.29% of the total consolidated assets, and the net sales of such companies represented 70.68% of the total consolidated net sales. The accounts of the subsidiary companies, whose records we did not examine, are included in the consolidated statements on the basis of company reports which were reviewed by us.

In our opinion, based upon the examination and review outlined in the preceding paragraph, the accompanying consolidated balance sheet and related statement of consolidated profit and loss fairly present, in accordance with accepted principles of accounting which have been consistently maintained during the period under review (except for a change in the basis for determining the provision for Federal income tax as indicated in the report to stockholders), the financial position of the companies at January 31, 1937 and the results of their operations for the year ended that date.

ARTHUR ANDERSEN & CO.

New York, N. Y.,
April 15, 1937.